

The Graphic Arts Machinery and Equipment Exemption extends to machinery and equipment that is used primarily (more than 50% of the time) in graphic arts production. See 86 Ill. Adm. Code 130.325. (This is a PLR.)

March 24, 1999

Dear Xxxxx:

This Private Letter Ruling, issued pursuant to 2 Ill. Adm. Code 1200 (see enclosed), is in response to your letters of May 28, 1998 and February 25, 1999. Review of your request for a Private Letter Ruling disclosed that all information described in paragraphs 1 through 8 of subsection (b) of the enclosed copy of Section 1200.110 appears to be contained in your request.

In your May 28, 1998 letter, you have stated and made inquiry as follows:

On behalf of our client, COMPANY, we are submitting this request for a private letter ruling concerning the application of the Retailers' and Service Occupation Taxes ('ROT' and 'SOT') to a particular fact pattern. An executed Power of Attorney is attached authorizing us to represent COMPANY, an Illinois corporation, in securing the requested private letter ruling.

I. Facts

Our client, COMPANY ('COMPANY'), operates a printing and direct mailing preparation service facility located at ADDRESS, Illinois. COMPANY provides a number of products to its customers. The subject of this ruling request is the applicability of the ROT and SOT to machinery and equipment used by COMPANY in creating one of its products called PRODUCT.

PRODUCT is produced primarily by the NAME newspaper, which is the parent corporation of COMPANY. PRODUCT, which resembles a daily newspaper, is distributed to residences usually twice per week. PRODUCT consists of a cover, known as a 'wrap' and various advertising supplements inserted into the wrap. The wrap is in the form of a newspaper and contains the NAME banner and various articles, stories or classifieds which are of interest to the general public. The wrap is produced by the NAME and delivered to the CITY facility of COMPANY. The advertising supplements are also shipped to COMPANY's facility by the advertisers seeking to place their advertising in PRODUCT.

Once wraps and advertising supplements are received by COMPANY, COMPANY is responsible for assembling, addressing and distributing the final product. To create PRODUCT, the wraps and advertising supplements are positioned on equipment that is attached to on-line insertion machines. The on-line insertion machines collate or

assemble the wrap with the advertising supplements. The on-line insertion machines (collators) operate as an integral component of the production process. The printed wrap is fed into the insertion machine. The advertising supplements are selectively inserted into the wrap as the wrap moves along the insertion machine. Once the collating process is finished, an address is ink-jet printed onto the exterior of the wrap. Address information is maintained in a data base that is interfaced with the machinery and equipment to permit high-speed production. Finished PRODUCT are then delivered to a U.S. Postal facility where they are mailed to residences.

II. Rulings Requested

We respectfully request the following rulings from the Department:

1. The production of PRODUCT by COMPANY is graphic arts production as that term is defined by Section 2-30 of the Retailers' Occupation Tax.
2. The purchase of the following machinery and equipment, used primarily in graphic arts production, qualifies for the Graphic Arts Machinery and Equipment Exemption:
 1. Feeder - Feeds the wraps into the videojet printer.
 2. Insertion Machine (Collator) - Collates or gathers advertising supplements and inserts the advertising supplements into the wrap

III. Legal Analysis

A. Statement of Authorities Supporting Taxpayer's Views

The operations conducted by COMPANY qualify as graphic arts production. The machinery and equipment used by COMPANY primarily in that graphic arts production qualifies for the graphic arts machinery and equipment exemption from the Retailers' Occupation Tax. Section 2-30 of the Retailers' Occupation Tax ('the ROT') defines graphic arts production as '...printing by one or more of the common processes or graphic arts production services as those processes and services are defined in Major Group 27 of the U.S. Standard Industrial Classification Manual.' As you know, Section 2-5(4) of the ROT provides an exemption from the ROT for the purchase of:

Graphic Arts machinery and equipment, including repair and replacement parts, both new and used, and including that manufactured on special order or purchased for lease, certified by the purchaser to be used primarily for graphic arts production.

The Department has adopted rules governing the graphic arts machinery and equipment exemption (86 Ill. Adm. Code 130.325). Section 130.325(b)(1) of the Department's rules quotes Section 2-30 of the ROT and then further provides:

The exemption includes printing by letterpress, lithography, gravure, screen, engraving and flexography and includes such printing trade services as typesetting, negative production, plate production, bookbinding, finishing, looseleaf binder production and other services set forth in Major Group 27. The exemption extends only to machinery and equipment used in the act of production. Accordingly, no other type or kind of tangible personal property will qualify for the exemption, even though it may be used primarily in the graphic arts business.

COMPANY's operations are classified under Major Group 27 of the Standard Industrial Classification Code, Industry No. 2791 'Typesetting' and Industry No. 2759 'Commercial Printing, Not Elsewhere Classified.' COMPANY engages in the following printing activities which make up this Industry No. 2759: 1) Gummed labels and seals, printed: except lithographed or gravure; 2) Labels printed: except lithographed or gravure printing, and 3) Printing, commercial or job except lithographic or gravure.

Address data is printed either directly onto the wraps, or onto gummed labels that are affixed to the wraps. As indicated in the preceding paragraph, the printing of labels is classified as a printing activity under Major Group 27 of the Standard Industrial Classification Code. Therefore, pursuant to Section 2-30 of the ROT, this activity constitutes graphic arts production.

In Private Letter Ruling ST 90-0742, the Department recognized that the graphic arts machinery and equipment exemption extends to equipment to collate bind or finish the graphic arts product and the exemption could be claimed by a company that cuts and folds the printed work of a customer.

Section 130.325c)(3) of the graphic arts machinery and equipment rules of the Department provides examples of various types of 'activities' that are considered an exempt use of machinery and equipment. The rule states that this list is provided by way of illustration and not limitation. The list includes at subsection c)(3)C) 'equipment to collate, bind or finish the graphic arts product.'

As indicated in Section 100.325 of the Department's rules, equipment used to collate, bind or finish the graphic arts product constitutes an exempt use. Folders are specifically addressed in General Information Letter ST 94-0548.¹ In 94-0548 the Department was asked to provide advice concerning whether a sheet fed folder machine would qualify for exemption from the state's sales and use tax. In its response to the taxpayer the Department referenced the graphic arts machinery and equipment exemption from the Retailers' Occupation Tax. The Department stated '[t]he sheet fed

folder machines you sell may qualify for the exemption depending upon if the purchaser primarily uses the machine in an exempt process.' Likewise the use of insertion machines is addressed in Private Letter Rulings 92-0593 and 90-0527. These rulings state that the graphic arts machinery and equipment exemption applies to on-line insertion machines that collate advertising sections of a newspaper and the newspaper itself.

B. Statement of Authorities Contrary to the Taxpayer's Views

We are unaware of any rulings by the Department that hold that feeders and insertion machines are not machinery that qualifies for the graphic arts machinery and equipment exemption.

IV. Information Required by 2 Ill. Adm. Code 1200.110(b)

This private letter ruling request is for the current tax period and any open period for which a claim for refund might be filed with respect to machinery and equipment found to be exempt under the ROT for which tax has been erroneously been paid by COMPANY. No audit or litigation is pending with the Department on the subject of this private letter ruling request.

To the best of the knowledge of COMPANY and Grant Thornton, LLP the Department has not previously ruled on the same or a similar issue for the taxpayer or a predecessor. The taxpayer or any representatives has not previously submitted the same or a similar issue to the Department but withdrew it before a letter ruling has been issued.

Please feel free to contact me at your convenience if I may provide you with any additional information, or if you have any questions about this ruling request. I would also be happy to meet with you at your convenience to discuss this ruling request if you feel that it would be helpful.

In your February 25, 1999 letter you have stated the following:

In response to our recent telephone conversation, I am submitting this supplement to our private letter ruling request of May 28, 1998. This letter is designed to supplement and clarify the facts presented on behalf of our client COMPANY.¹

In our letter of May 28, 1998, we requested that the Department rule that certain machinery and equipment used by COMPANY in creating one of its products called 'PRODUCT' qualifies for the graphic arts machinery and equipment exemption. In our earlier letter we described the production process, and the machinery and equipment used in the process, as follows:

Once wraps and advertising supplements are received by COMPANY, COMPANY is responsible for assembling, addressing and distributing the final product. To create PRODUCT, the wraps and advertising supplements are positioned on equipment that is attached to on-line insertion machines. The on-line insertion machines collate or assemble the wrap with the advertising supplements. The on-line insertion machines operate as an integral component of the production process. The printed wrap is fed into the insertion machine. The advertising supplements are selectively inserted into the wrap as the wrap moves along the insertion machine. Once the collating process is finished, an address is ink-jet printed onto the exterior of the wrap. Address information is maintained in a data base that is interfaced with the machinery and equipment to permit high-speed production. Finished PRODUCT are then delivered to a U.S. Postal facility where they are mailed to residences.

After providing this description, we requested that the Department rule that the following described machinery and equipment qualifies for the Graphic Arts Machinery and Equipment exemption:

1. Feeder - Feeds the wraps into the videojet printer.
2. Insertion Machine (Collator) - Collates or gathers advertising supplements and inserts the advertising supplements into the wrap.

After further review of this description and discussion of this description with our client, COMPANY, it appears that this description is a bit misleading with respect to what has been described above as a 'feeder.' What was described as a 'feeder' above, is in actuality a component of the insertion machine.

COMPANY uses an insertion machine known as an NP630 Newspaper Inserter. As described in our earlier letter, the Inserter collates and assembles the wrap with the various advertising supplements that are components of the finished PRODUCT. I have attached a copy of the product specification sheets for the insertion machine for your review and information.

As noted on page 3 of the production specification material, the various components of the final PRODUCT are contained in 'hoppers.' These hoppers contain the different sections of the PRODUCT product and the sections are fed one at a time into the wrapper. The number of hoppers that are part of the insertion machine and the number of hoppers used in putting together a particular PRODUCT product are a function of the number of different components used in a particular PRODUCT. For example, COMPANY has address information that allows it to determine whether a particular residence is a single family home or an apartment. As a result, it will tailor the particular

components of the PRODUCT product to be mailed to a single family residence to include advertisements from home improvement or building materials retailers, and not include such advertisements in PRODUCT products mailed to apartment dwellers.

In the portion of our earlier letter quoted above, I mistakenly indicated that there is some type of separate feeder machine, that has as its function the feeding of wraps in a videojet printer for printing of the address information. This was incorrect. As described above, and as described in the attached product specific sheets, there is one newspaper insertion machine with various hopper components that is used to put together the PRODUCT Product. Upon completion of the insertion process, the finished PRODUCT product is fed from the insertion machine directly to the ink-jet printer. There is no separate machine known as a feeder that is used to feed the PRODUCT product from the insertion machine to the printer.

Therefore, we are respectfully requesting that the Department rule that the newspaper insertion machine used by COMPANY, including the component parts of that machine known as the 'hoppers,' qualifies for the Graphic Arts Machinery and Equipment Exemption.

I hope this provides clarification of my earlier letter. Please let me know if you have any additional questions with respect to this request for a ruling.

We have enclosed a copy of 86 Ill. Adm. Code 130.325, which is the Department's regulation for the Graphic Arts Machinery and Equipment Exemption. The Graphic Arts Machinery and Equipment Exemption extends to machinery and equipment that is used primarily (more than 50% of the time) in graphic arts production. "Graphics Arts Production" means printing by one or more of the common processes or graphic arts production services as those processes and services are defined in Major Group 27 of the U. S. Standard Industrial Classification Manual.

Our review of the NP 630 insertion machine as set out in your letters and the attached specification sheets shows that it performs different functions. The function or operation of feeding the PRODUCT product to the printer would not qualify as an exempt activity under the exemption because the feeding process is neither collating nor binding. However, the activities of the machine of collating and inserting the supplements into the newspapers would qualify for the exemption.

In viewing the operation of this machine in its totality, we conclude that its primary purpose is the collating function and it can qualify for the graphic arts machinery and equipment exemption if used primarily in the process as stated.

I hope this information is helpful. If you have further questions, please feel free to contact the Department.

Very truly yours,

George Sorensen
Associate Chief Counsel
Sales & Excise Tax

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Enc.

¹ We are aware that according to 2 Ill. Adm. Code 1200.120, '[g]eneral Information letters do not constitute statements of agency policy that apply, interpret or prescribe the tax laws administered by the Department. Information letters are not binding on the Department, may not be relied upon by taxpayers in taking positions with reference to tax issues and create no rights for taxpayers under the Taxpayers' Bill of Rights Act.' However, even though general information letters are not binding on the Department, they are a valuable source of information on the Department's thinking on a particular issue and when considered in conjunction with the statutes and rules of the Department can provide assistance to taxpayers in attempting to conform their activities to the requirements of the law and rules.

¹ Since the time of our original request, the company name has been changed from 'COMPANY' to 'Tribune Direct.' The entity itself has not changed; only the name.